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UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

FTC COMMERCIAL CORP., a California corporation,

Plaintiff,

vs.

M & C APPAREL GROUP, INC., a California corporation; RIAN D. GONZALEZ, an individual; ARMEN GREGORIAN, an individual; MIKE & CHRIS, LLC, a California limited liability company; GREEN MOCHI, LLC, a California limited liability company,

Defendants.

Case No. 08-CV-08431 GAF

OPPOSITION TO DEFENDANTS GREEN MOCHI, LLC, ARMEN GREGORIAN AND MIKE & CHRIS, LLC'S MOTION TO DISMISS PLAINTIFF'S FIRST AMENDED COMPLAINT PURSUANT TO FRCP 12(b)(6) OR ALTERNATIVELY TO STAY THIS ACTION OR REFER TO THE BANKRUPTCY COURT

[Declaration of Andrew V. Jablon and Request for Judicial Notice Filed Concurrently]

Date: April 6, 2009
Time: 9:30 a.m.
Crtrm.: 740

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MEMORANDUM OF POINTS AND AUTHORITIES

I. INTRODUCTION

Non-debtor defendants Armen Gregorian, Mike & Chris, LLC, and Green Mochi LLC (collectively the "Non-Debtor Defendants") have filed the instant Motion to Dismiss, or Alternatively to Stay or Transfer (the "Motion") based on a fundamental misrepresentation regarding Plaintiff's claims. Specifically, the Non-Debtor Defendants misrepresent the claims against them in an effort to: (1) shoehorn themselves into the automatic stay provisions of 11 U.S.C. § 362; and (2) argue that the First Amended Complaint ("FAC") fails to state sufficient facts to set forth a claim for relief.[1] As will be discussed below, the Motion must be denied as the claims against the Non-Debtor Defendants do not implicate the bankruptcy estate of either M&C Apparel Group, Inc. ("M&C Apparel") or non-defendant Michelangelo Gonzales ("Mike"), and the FAC properly sets forth each of the claims against the Non-Debtor Defendants.

II. LEGAL ARGUMENT

A. The Instant Action Does Not Violate The Automatic Stay: FTC Is Seeking To Recover *Its* Property, And Enforce *Its* Rights Against The Non-Debtor Defendants

The Non-Debtors initially argue that the Motion must be granted, and the action dismissed, because the filing and maintenance of the instant action violates the 11 U.S.C. § 362 automatic stay. (Motion, 5:22 – 7:11.) The automatic stay

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[1] The parties did meet and confer as to the original complaint in December, 2008 regarding the issue of the bankruptcy and whether Plaintiff had standing in light of the bankruptcy. In violation of Local Rule 7, however, the Non-Debtor Defendants failed to meet and confer regarding their arguments that the FAC failed to state a claim for reasons other than standing. (Declaration of Andrew V. Jablon, ¶ 2.)

provisions of 11 U.S.C. § 362, however, apply only to debtors, and not to their co-defendants. *In re Miller*, 262 B.R. 499 (9th Cir. BAP 2001); *Chugach Forest Products, Inc.*, 23 F.3d 241 (9th Cir. 1994); *United States v. Dos Cabezas Corp.*, 995 F.2d 1486 (9th Cir. 1993); *Seiko Epson Corp. v. Nu-Kote Int'l, Inc.*, 190 F.3d 1360, 1364 (Fed. Cir. 1999). In *Miller*, the Ninth Circuit held that "Section 362(a)(1) applies only to actions against a debtor", and allowed discovery to continue against a bankrupt party, as long as the discovery was related to the claims against the other defendants. *In re Miller*, 262 B.R at 503. Simply put, "section 362(a) does not stay actions against guarantors, sureties, corporate affiliates, or other non-debtor parties or their property." *In re Chugach*, 23 F. 3d at 246 (quoting *In re Advanced Ribbons & Office Prods.*, 125 B.R. 259, 263 (9th Cir. BAP 1991)).

There is absolutely *no* authority prohibiting Plaintiff's prosecution of its claims against Non-Debtor Defendants arising out of property to which the bankrupt estate(s) have no legal or equitable interest. *See*, *Matter of Boyd*, 11 F.3d 59, 61 (5th Cir. 1994) (bankruptcy petition filed after extinguishment of debtor's rights to foreclosed property had no effect on foreclosed property). Moreover, "it is clearly established that the automatic stay does not apply to non-bankrupt co-defendants of a debtor 'even if they are in a similar legal or factual nexus with the debtor.'" *Seiko Epson Corp.*, 190 F.3d at 1364 (quoting *Maritime Elect. Co. v. United Jersey Bank*, 959 F.2d 1194, 1205 (3rd Cir. 1991)).

Accordingly, the Non-Debtor Defendants' reliance on *Amedys v. National Century Fin. Enters., Inc.* 423 F.3d 567 (6th Cir. 2005) is misplaced. In *Amedys* the creditor sued the debtor's bank to recover the *debtor's* funds in possession of the bank. Moreover,

> the focus of the inquiry under § 362(a)(3) is on whether a judgment against the solvent codefendants would actually deplete the bankruptcy estate. *National Century*, 423 F.3d at 579 (citing, *Patton* 8 F.3d at 349).

In re Cincom iOutsource, Inc., 398 B.R. 223 (Bankr. S.D. Ohio 2008).

Here, Plaintiff is not seeking to recover the Debtors' funds from the Non-Debtor Defendants. On the contrary, as discussed below, on the face of the FAC, and as supported by the admissible evidence before the Court, Plaintiff is seeking to prosecute *direct* claims against Non-Debtor Defendants for their interference with property which belongs to Plaintiff and in which Plaintiff has a *direct* interest. As such, a judgment against the Non-Debtor defendants would *not* deplete either of the bankruptcy estates as the evidence before the Court establishes that neither estate has a legal or equitable interest in the subject property.

1. The Non-Debtor Defendants Have The Burden Of Proof In Convincing The Court To Exercise Its Authority To Determine The Applicability Of The Automatic Stay

> Whether the stay applies to litigation otherwise within the jurisdiction of a district court or court of appeals is an issue of law within the competence of both the court within which the litigation is pending [citations] . . . The court in which the litigation claimed to be stayed is pending has jurisdiction to determine not only its own jurisdiction but also the more precise question whether the proceeding pending before it is subject to the automatic stay.

In re Baldwin-United Corp. Litigation, 765 F.2d 343, 347 (2d Cir. N.Y. 1985). Cited to with approval by *Lockyer v. Mirant Corp.*, 398 F.3d 1098, 1106 (9th Cir. 2005) ("[A] district court has jurisdiction to decide whether the automatic stay applies to a proceeding pending before it, over which it would otherwise have jurisdiction.)

Plaintiff has not been able to locate any cases directly addressing the burden of proof with respect to a Motion to Stay an action under 11 U.S.C. § 362.

Nonetheless, where Courts have addressed the propriety of a stay generally, the burden has fallen squarely on the party seeking the stay to establish its legal, factual, and equitable support. For example, in seeking an equitable stay under *Landis v. North American Co.*, 299 U.S. 248 (1936), the party who seeks the stay bears the burden of showing hardship or inequity in being forced to move forward if there is "even a fair possibility that the stay for which he prays will work damage to someone else." *Lockyer*, 398 F.3d at 1109 (9th Cir. 2005); *Jones v. Clinton*, 72 F.3d 1354, 1364 (8th Cir. 1996) ("Traditionally, an applicant for a stay has the burden of showing specific hardship or inequity if he or she is required to go forward."). Similarly, in a Motion for Relief from Stay under 11 U.S.C. § 362, with the exception of whether the debtor has equity in the challenged asset(s), the party *opposing* relief from stay bears the burden of proof and persuasion.

> (g) In any hearing under subsection (d) or (e) of this section concerning relief from the stay of any act under subsection (a) of this section--
>
> (1) the party requesting such relief has the burden of proof on the issue of the debtor's equity in property; and
>
> (2) the party opposing such relief has the burden of proof on all other issues.

Since Defendants are in the same position as a party opposing a Plaintiff's pursuit of calims outside bankruptcy, it follows, therefore, that *Defendants* have the burden of proving that the 11 U.S.C. § 362 automatic stay applies to the present action – a burden they have completely failed to meet.

2. <u>The FAC Alleges Sufficient Facts To Establish Standing</u>

Initially, the Non-Debtor Defendants mischaracterize the FAC, claiming that the causes of action against them concern property of M&C Apparel and deceitfully claiming that the property is expressly alleged in the FAC to be "M&C Apparel's"

property. The Non-Debtor Defendants' claim is transparently false and blatantly misconstrues the allegations of the FAC.

Defendants disingenuously cite to Paragraphs 11 and 95[2] of the FAC for the proposition that this action seeks, as to the Non-Debtor Defendants, "recovery of property of a bankruptcy estate." The paragraphs cited by the Non-Debtor Defendants simply set forth the undisputed fact that M&C Apparel granted a security interest to Plaintiff in all of its tangible and intangible property, including after acquired property. (FAC, ¶ 11 (quoting language of the underlying factoring agreement); ¶ 96 ("[a]s discussed above, FTC acquired a security interest in, among other things, the Trademark as part of the FTC Agreements. . . . ").) The Non-Debtor Defendants simply ignore that the FAC unambiguously sets forth that the secured collateral, defined in ¶ 11 of the FAC, was *surrendered to Plaintiff* prior to M&C Apparel or Mike filing for bankruptcy protection. (FAC, ¶¶ 27-29.) Accordingly, the FAC makes clear that *Plaintiff* is the lawful owner of the subject property.

3. <u>The Evidence Before The Court Establishes That The FAC Seeks Recovery Of *Plaintiff's* Property</u>

The Non-Debtor Defendants further challenge the FAC on the grounds that it violates the automatic stay by attempting to submit evidence that the Bankruptcy Court has already determined that the subject property belongs to the bankruptcy estate. Initially, all of the purported evidence submitted by the Defendants is inadmissible for the reasons set forth in the concurrently filed *Evidentiary Objections to Defendants' Request For Judicial Notice*. Moreover, the Non-Debtor Defendants "evidence" has been grossly distorted in an attempt at misleading the

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[2] Plaintiff assumes that the Non-Debtor Defendants meant Paragraph 96, as Paragraph 95 only incorporates by reference Paragraphs 1 – 41 of the FAC.

Court.

First, the Non-Debtor Defendants disingenuously argue that the February 3, 2009 *Ex Parte* Application by the Bankruptcy Trustee to sell the subject property supports their position as it "is supported by a Stipulation for sale signed by Plaintiff." (Motion (6:22-24.) The Motion ignores that the Stipulation *expressly provides*:

> 9. The Parties further agree that the Court's approval of this Sale Stipulation shall in no way whatsoever be construed as a determination that the Property is or is not property of the estate.

(*Plaintiff's Request for Judicial Notice In Support Of Its Opposition To Defendants' Motion To Dismiss* ("RJN"), ¶ 6, Stipulation Among Debtor, FTC Commercial Corp. And Chapter 7 Trustee Re Sale Of Personal Property.) Plaintiff's position has been consistent – it owns the subject property. The Stipulation (and *ex parte* Application) was necessary simply because the Non-Debtor Defendants were still in possession, custody, or control of the items, and it was the only way which possession of these depreciating assets could be acquired and the goods sold in an expeditious fashion.

Continuing their attempt at deception, the Non-Debtor Defendants (without regard to the rules of evidence) point to an unauthenticated purported website printout of a *tentative* ruling by the Bankruptcy Court, that was never adopted. There is no authority for the Court to take judicial notice of another Court's *tentative* ruling that was never adopted. Moreover, even if treated like an actual Order, non-Debtor Defendants ignore the fact that a court may take judicial notice of a document filed in another court "not for the truth of the matters asserted in the other litigation, but rather to establish the fact of such litigation and related filings." *Kramer v. Time Warner Inc.*, 937 F.2d 767, 774 (2nd Cir. 1991); *Taylor v. Charter Med. Corp.*, 162 F.3d 827, 829-830 (5th Cir. 1998). Thus, while a court may

judicially notice another court's order, it may not accept that court's "findings of fact" as true. *Wyatt v. Terhune*, 315 F.3d 1108, 1114 (9th Cir. 2003); *United States v. Jones*, 29 F.3d 1549, 1553 (11th Cir. 1994); *Lee v. City of Los Angeles*, 250 F.3d 668, 690 (9th Cir. 2001).

Further, the Non-Debtor Defendants fail to acknowledge that Plaintiff has already obtained a ruling in this action (while it was in the Los Angeles Superior Court), based on *admissible* evidence that *the subject property belongs to Plaintiff*. *See*, RJN, ¶¶ 1-3. Unlike the *tentative* order, in a separate action, cited above, this prior ruling is from this action.

The declarations submitted by Plaintiff in support of its Applications for Writ of Attachment and Writ of Possession (RJN, ¶ 4), which are incorporated herein by reference, establish, by way of admissible evidence, that Plaintiff has standing to bring this action against the Non-Debtor Defendants, and that Plaintiff is the lawful owner of the collateral in question. As these declarations remain uncontroverted by the Non-Debtor Defendants, the Motion must be denied.

4. Plaintiffs Should Be Afforded The Right To Complete Discovery On Issues Related To The Proposed Stay

In the event that the Court is inclined to grant the Non-Debtors' Motion to Stay the action under 11 U.S.C. § 362, Plaintiff requests the opportunity to complete discovery into the issues addressing the stay and leave to submit supplemental briefing. If the Court finds that 11 U.S.C. § 362 applies, Defendants will then argue that the Court's finding adjudicates that Plaintiff's claims and property belong to the estate(s), and Defendants will seek to bar an adversarial proceeding by Plaintiff in the Bankruptcy Court. Although Plaintiff does not believe this would be a factually or legally proper result, Plaintiff should be given the opportunity to conduct discovery now necessary to demonstrate the propriety of its claims and the inapplicability of the automatic stay provisions. Specifically, Plaintiffs seek to:

(1) complete the deposition of Green Mochi, LLC's principal,

Armen Gregorian;

(2) take the deposition of Carmella Parungao, a Green Mochi, LLC's employee and M&C Apparel's former Chief Financial officer;

(3) take the deposition of M&C Apparel's former accountants; and

(4) conduct certain focused written discovery establishing the inapplicability of the automatic stay.

Between the foregoing discovery and the scheduled deposition of two Green Mochi, LLC employees on March 18 and 19, 2009, both of which are believed to have information relevant to the issues presented herein, Plaintiff is confident that supplemental briefing would further confirm that FTC owns the subject assets.

B. The First Amended Complaint Properly Alleges Each Of Its Claims For Relief

1. Plaintiff Has Standing To Bring Each Of Its Claims

For purposes of the 12(b)(6) component of the instant Motion, including the challenge to Plaintiff's standing, all of the allegations of material fact in the FAC must be "taken as true and construed in the light most favorable to the nonmoving party." *Hydranautics v. Filmtec Corporation*, 70 F.3d 533, 536 (9th Cir. 1995). Further, the "Court must . . . draw all reasonable inferences in favor of the non-movant; it should not dismiss the complaint unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Twentieth Century Fox Film Corporation v. Marvel Enterprises, Inc.*, 220 F.Supp.2d 289, 292 (S.D.N.Y. 2002) (internal quotations omitted). On the face of the FAC, the detailed factual allegations regarding the surrender of the secured collateral (FAC, ¶¶ 27-29) defeat the Motion to Dismiss based on lack of standing. *See Sacks v. Office of Foreign Assets Control*, 466 F.3d 764, 771(9th Cir. 2006) (cited by the Non-Debtor Defendants at Motion, 5:4-5, and holding that, "[t]o survive a Rule 12(b)(6) motion to dismiss, [plaintiff] must allege facts in his Amended Complaint that, if proven, would confer standing upon him.")

As discussed above, contrary to Defendants' allegations, the claims against the Non-Debtor Defendants' do *not* seek the recovery of property of a bankruptcy estate. As discussed, the FAC expressly alleges that the assets in question *belong to Plaintiff*. The key allegations for the present Motion are found in paragraphs 27 through 29, which unambiguously set forth that the secured collateral, defined in ¶ 11 of the FAC, was *surrendered to Plaintiff* prior to M&C Apparel or Mike filing for bankruptcy protection. (FAC, ¶¶ 27-29.) Defendants' standing argument, therefore, fails as a matter of law.

2. <u>The Conversion Claim Is Properly Alleged</u>

To plead a claim for conversion, Plaintiff was required to allege: (1) ownership or right to possession of the property at the time of the conversion; (2) Defendants' conversion by a wrongful act or disposition of property rights; and (3) damages. *Shopoff & Cavallo LLP v. Hyon*, 167 Cal. App. 4th 1489, 1507 (2008). "It is not necessary that there be a manual taking of the property; it is only necessary to show an assumption of control or ownership over the property, or that the alleged converter has applied the property to his own use." *Id.* Here, the Non-Debtor Defendants contend that the FAC fails to set forth a claim for conversion because: (1) "all of the allegedly converted property belongs to either M&C Apparel or Gonzalez" (Motion 9:18-19); (2) "Plaintiff fails to plead any wrongful act or disposition of property rights by Defendants" (Motion, 9:26-27); and (3) "Plaintiff also fails to plead damages adequately". (Motion, 10:2-3.) The Non-Debtor Defendants' contentions, however, ignore the plain text of the FAC.

Contrary to the Non-Debtor Defendants' contention, the FAC does *not* allege that all of the converted property belongs to either M&C Apparel or Gonzalez. Rather, as discussed above, the FAC sets out that the converted property was subject to a recorded security interest (FAC, ¶ 11) and, as of November 3, 2008, was surrendered to Plaintiff. (FAC, ¶¶ 27-29.) These allegations are sufficient to establish for pleading purposes that Plaintiff owned the converted property.

Moreover, the FAC properly alleges a wrongful act – namely that, acting in concert with M&C Apparel, the Non-Debtor Defendants stole the subject property. (FAC, ¶¶ 37-40, 60.) Similarly, the FAC properly alleges damages (FAC, ¶¶ 62-66.) The Non-Debtor Defendants' apparent argument that the Plaintiff must itemize damages to the penny is simply not based in law. Plaintiff, by describing the categories of damages it has suffered, satisfies its pleading obligations.

Accordingly, as the FAC properly alleges the essential elements of a conversion claim for relief, the Motion must be denied.

3. <u>The Fraudulent Conveyance Claim Is Properly Alleged</u>

The Non-Debtor Defendants attack Plaintiff's Fourth Cause Of Action, for fraudulent conveyance, on the grounds that Plaintiff purportedly did not allege that the consideration for the conveyance was inadequate and that the grantee participated in the transaction with the intent to defraud the creditor. (Motion, 10:15-18.) Again, the Non-Debtor Defendants ignore the express allegations of the FAC.

Specifically, the FAC clearly sets forth that the consideration was inadequate at paragraphs 39 and 69, which describe how, purportedly in exchange for $84,130.66, M&C Apparel claimed to have transferred goods (the "On-Site Inventory") worth, at wholesale, more than five hundred thousand dollars ($500,000). Moreover, the FAC specifically alleges that the Non-Debtor Defendants had actual knowledge of:

1. M&C's debts to FTC;
2. FTC's security interest in, *inter alia*, the On-Site Inventory;
3. FTC's foreclosure on the On-Site Inventory; and
4. M&C's surrender of the On-Site Inventory.

(FAC, ¶¶ 36-41, 70.) Moreover, the FAC specifically alleges that the fraudulent conveyance scheme was perpetrated in an "attempt to secure a negotiating advantage over FTC in the on-going negotiations regarding the disposition of the

Collateral." (FAC, ¶ 71)

Additionally, the Non-Debtor Defendants, citing to *Kuhlman v. Pacific States Savings and Loan Company, et al.*, 17 Cal. 2d 820 (1941), assert that Plaintiff must allege that the grantee "participated in the transaction with the intent to defraud the creditor." (Motion, 10:17-18.) *Kuhlman*, however, does not limit a grantee's liability to situations in which it "intended" to defraud the creditor. Rather, the *Kuhlman* Court stated:

> A conveyance made for a valuable consideration may not be attacked by the grantor's creditor, even though the transaction was entered into by the debtor with intent to delay or defraud his creditors, **unless the grantee so intended or participated in *or had knowledge of* the fraudulent intent.**

Kuhlman, 17 Cal. 2d at 821-822 (emphasis added). Accordingly, the Non-Debtors' contention that the *Kuhlman* Court held that knowledge alone of the grantor's fraudulent intent was insufficient to state a claim for fraudulent transfer against the grantee is simply incorrect.

The allegations of the FAC, which set out in detail the Non-Debtor Defendants' knowledge of the fraudulent intent, and for that matter their participation in the fraud, more than satisfy the *Kuhlman* requirements and the requirements of *Fed. R. Civ. P.* 9(b).

4. <u>The Interference With Contract Claim Is Properly Alleged</u>

> The elements which a plaintiff must plead to state the cause of action for intentional interference with contractual relations are (1) a valid contract between plaintiff and a third party; (2) defendant's knowledge of this contract; (3) defendant's intentional acts designed to induce a breach or disruption of the contractual

> relationship; (4) actual breach or disruption of the contractual relationship; and (5) resulting damage.

Pacific Gas & Electric Co. v. Bear Stearns & Co., 50 Cal. 3d 1118, 1126 (1990).

> Because interference with an existing contract receives greater solicitude than does interference with prospective economic advantage (*Della Penna v. Toyota Motor Sales, U.S.A., Inc., supra*, 11 Cal. 4th at p. 392), it is not necessary that the defendant's conduct be wrongful apart from the interference with the contract itself. (*LiMandri v. Judkins, supra*, 52 Cal. App. 4th at p. 343.)

Quelimane Co. v. Stewart Title Guaranty Co. 19 Cal. 4th 26, 55 (1998). *See also, Metal Lite, Inc. v. Brady Constr. Innovations, Inc.*, 558 F. Supp. 2d 1084, 1094 (C.D. Cal. 2007) (quoting with approval *Quelimane Company, Inc. v. Stewart Title Guaranty Co.)* Here, the Complaint properly alleges each of the elements of the claim for interference with contract.

(a) <u>Plaintiff Alleges A Valid Contract Between Plaintiff And Third Parties</u>

The Non-Debtor Defendants mistakenly argue that there is no allegation of a contract between FTC and any third party alleged in the FAC. (Motion, 12:1-8.) Defendants ignore, however, that the FAC properly alleges that: (1) Plaintiff had a valid security interest in orders (i.e., Contracts) between M&C Apparel and third parties (the "Orders") (FAC, ¶¶ 25-26; (2) it foreclosed on its security interest in the Orders (FAC, ¶¶ 27-29). Accordingly, by virtue of the foreclosure, Plaintiff stood in the shoes of M&C Apparel with respect to the Orders, and a valid contract between plaintiff and third parties has been properly alleged.

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(b) Defendant's Knowledge Of The Orders And Intentional Acts Designed To Induce A Breach Or Disruption Of The Contractual Relationship Are Clearly Alleged

The FAC properly sets forth both knowledge and intentional acts designed to induce a breach or disruption in the contractual relationship represented by the Orders. Specifically, the FAC provides that:

> Additionally, Armen advised FTC that through one or more of their corporate entities, they were in process of fulfilling the Orders, using the stolen inventory, stolen order information, stolen patterns and design, and the Trademark, with the intent to ship to M&C's customers (the "Customers") the resulting product (the "Counterfeit Goods"). The Counterfeit Goods would be shipped by an entity (presumably the Successor LLC or Green) not, on its face, a party to the FTC Agreements. Armen specifically told Leon Neman, the president of FTC, that if FTC wanted to stop them from engaging in this conduct, FTC would have to file suit and seek an injunction.

(FAC, ¶ 40).

(c) Actual Breach Or Disruption Of The Contractual Relationship And Resulting Damage Is Adequately Pled

Actual breach or disruption of the contractual relationship arising out of the Orders is expressly alleged in the FAC. Specifically, the FAC sets forth that:

> Plaintiff is informed and believes, and based thereon alleges, that the Successor LLC, Armen, Green, and Does 2 through 10, and each of them, have or are in the process

> of purporting to fill the Orders and ship to the Customers in direct interference with FTC's right as the holder of a possessory interest in the Orders.

(FAC, ¶ 88). Similarly, damage resulting from the interference is alleged in the FAC:

> As a direct, foreseeable and proximate result of interference by the Successor LLC, Armen, Green, and Does 2 through 10, as alleged herein, FTC has been damaged in an amount that is currently unknown, but which shall be proven at trial, and is estimated at no less than one million dollars ($1,000,000).

(FAC, ¶ 89.)

Having pled all of the requisite elements of a claim for interference with contractual relationships, the Motion must be denied.

5. <u>The Trademark Infringement Claims Are Properly Alleged</u>

The Non-Debtor Defendants assert that, as to the Seventh and Eighth Causes of Action for Trademark Infringement, Plaintiff has "failed to allege facts to establish its purported interest in the MIKE&CHRIS trademark, and thus have no standing to bring trademark infringement claims against Defendants." (Motion, 12:25-27) Specifically, the Non-Debtor Defendants assert that because the United States Patent and Trademark Office ("USPTO") website purports to show Mike as the owner of the MIKE&CHRIS trademark (the "Trademark"), Plaintiff did not take a security interest in the mark, and thus lacks standing.

Initially, the Non-Debtor Defendants' reliance on the purported USPTO website printout is misplaced. The printout, which is inadmissible, demonstrates nothing other than, at most, the absence of a *recorded* assignment of the Trademark. A trademark assignment – which Plaintiff is informed and believes occurred when Mike transferred assets from the sole proprietorship to the M&C Apparel entity –

does not have to be recorded to be effective. *American Manufacturing Company, Inc. v. Phase Industries, Inc.*, 192 U.S.P.Q. (BNA) 498, 500 (Trademark Trial & App. Bd. 1976) ("Neither a formal assignment nor recordation of an assignment in the Patent and Trademark Office is necessary to pass title or ownership to common law or statutory trademark rights.")

The express allegations of the FAC , which, as noted above, must be "taken as true and construed in the light most favorable to the nonmoving party" (*Hydranautics*, 70 F.3d at 536) are more than sufficient to set forth standing to bring the trademark infringement claims. Specifically, the FAC asserts that:

1. Mike, individually and on behalf of M&C Apparel, as well as other representatives of M&C Apparel, repeatedly represented that M&C Apparel owned the Trademark (FAC, ¶ 38 and 96);

2. The Trademark was (prior to foreclosure by Plaintiff) owned by M&C Apparel (FAC ¶ 96);

3. Plaintiff took a security interest in the MIKE&CHRIS trademark (the "Trademark") (FAC, ¶ 11 and 17); and

4. The secured collateral was surrendered to Plaintiff (FAC, ¶¶ 27-28).

Accordingly, the Motion must be denied.

6. <u>Misappropriation Of Trade Secrets</u>

(a) <u>The FAC Properly Pleads Misappropriation of Trade Secrets.</u>

Defendants correctly state the elements of a misappropriation of trade secrets claim: (1) the plaintiff is the owner of a trade secret; (2) the information was a trade secret at the time of the misappropriation; (3) defendants improperly acquired the trade secret; (4) plaintiff has been damaged by the misappropriation; and (5) the defendant's acquisition was a substantial factor in causing that damage. *See, e.g.*, Cal. Civ. Jury Instructions No. 4401. As the FAC pleads each of these elements,

rather than actually challenging the sufficiency of the pleading, the Non-Debtor Defendants' motion argues that FTC cannot prove its claim. This is improper, and its motion should be denied.

(i) The FAC Pleads that FTC Owned the Customer List and Pending Order Information, Which are Trade Secrets.

A trade secret is information that "(1) derives economic value, actual or potential, from not being generally known to the public or to other persons who can obtain economic value from its disclosure or use; and (2) is the subject of efforts that are reasonable under the circumstances to maintain its secrecy." *Cal. Civ. Code* § 3426.1(d). The FAC here identified two trade secrets: (1) M&C's customer list, and (2) its in-process orders. [FAC ¶ 115.] California has specifically recognized that such information can qualify for trade secret protection. *See Morlife, Inc. v. Perry*, 56 Cal. App. 4th 1514, 1522 (1997). *Morlife* found that a customer list can be a trade secret "because its disclosure would allow a competitor to direct its sales efforts to those customers who have already shown a willingness to use a unique type of service or product as opposed to a list of people who only might be interested."

Here M&C's customer list, and its list of in-process orders, provides the same information. *Morlife* further demonstrated why the listing of retailers on M&C's website does not preclude the customer list from being a trade secret. *Morlife* explained that the customers list was a trade secret, in part, because of "the difficulty encountered by sales personnel in getting past the 'gatekeepers' and identifying and gaining access to the actual decision makers with the authority to purchase [goods.]" *Id.* Here, the non-public, protected, information from the customer list and in-process orders provides the same type of information: who the decision makers are at the various retailers, information on how to contact them, how much they have bought in the past, and on what terms. Using this information would allow the

Defendants to "to solicit both more selectively and more effectively." *Morlife*, 56 Cal. App. 4th at 1522. That is exactly what Defendants have done – stealing the in-process orders and attempting to fulfill the orders themselves. [FAC ¶¶ 39-41.] As pleaded, the FAC has identified trade secrets protectable under California law.

The FAC further alleges that FTC owns the trade secrets by specifically alleging that no later than November 14, 2008, FTC had foreclosed on the Collateral, including the Trade Secrets. [FAC ¶¶ 28-35.] Thus, the FAC alleges that FTC owned the Collateral, including the Trade Secrets as of November 14, 2008 at the latest. [*See id.*, ¶ 116.] FTC has therefore alleged that it owns the Trade Secrets.

(ii) The FAC alleges misappropriation by Defendants.

Defendants merely quibble with the exact language used by the FAC. The FAC alleges that, following FTC's foreclosure on, and M&C's surrender of, the Collateral, including the Trade Secrets, the Defendants had no right to possess or use the customer list, and did so wrongfully. [FAC ¶ 124.] The FAC further alleges that Defendants have wrongfully attempted to use those trade secrets. [*Id.* at ¶¶ 39-41.] California has found such use to be improper. *Golden State Linen Service, Inc. v. Vidalin*, 69 Cal. App. 3d 1, 7-8 (1977) (holding that "information relative to customers (e.g., their identities, locations, and individual preferences), obtained by a former employee in his contacts with them during his employment, may amount to "trade secrets" which will warrant his being enjoined from exploitation or disclosure after leaving the employment."). Thus, the FAC properly pleads the Defendants' misappropriation.

(iii) The FAC properly alleges causation and damages.

Defendants argue that FTC must plead (1) a reasonable basis for its damages claim, and (2) facts to establish that Defendants' conduct was a substantial cause of

the damages. Defendants fail to cite any authority for those propositions because there is none. To survive a motion to dismiss, all FTC needed to plead is the fact of damage, and that the Defendant was a substantial factor in causing it. *See Enron Oil Trading & Transp. Co. v. Walbrook Ins. Co.*, 132 F.3d 526, 529 (9th Cir. 1997) (holding that a plaintiff is "not required to allege in its complaint the evidentiary facts in support of its theory of recovery."). The FAC pleads exactly these elements. [*See* FAC ¶ 126.]

7. <u>The Unfair Competition Claim Is Properly Alleged</u>

The Non-Debtor Defendants seek to strike Plaintiff's claim for common law unfair competition on the basis that Plaintiff failed to allege "passing off". Specifically, the Motion asserts that

> "[t]he basis of Plaintiff's claim is that Defendants purportedly ***misappropriated*** the "collateral," not that it was "passing off" Defendants' goods for those of M&C Apparel. Plaintiff alleges in the Amended Complaint that Defendants were selling the ***actual goods*** of M&C Apparel, not imitation goods made to appear as genuine, as required by a claim for passing off."

(Motion, 16:20-23). Defendants' analysis of the FAC is fundamentally flawed, as it conflates two separate wrongs – the theft and subsequent sale of Collateral (FAC, ¶¶ 39, 43-51), and the manufacture and sale of counterfeit goods.

The FAC set forth several critical allegations in support of the unfair competition claim:

1. Non-Debtor Defendants are selling garments which improperly bear the Mike & Chris trademark (Cite) (the "Counterfeit Garments");

2. The Counterfeit Garments are being manufactured by the Non-Debtor Defendants using M&C Apparel's patterns, designs, and markers which belong to FTC (by virtue of the foreclosure/surrender) (FAC, ¶ 28, 40-41, 96-111); and

3. The Counterfeit Garments are being sold by the Non-debtor Defendants to customers in "fulfillment" of orders which were placed with M&C Apparel, and which belong to FTC (by virtue of the foreclosure/surrender) (FAC, ¶ 28, 40).

Accordingly, the FAC has properly set forth the necessary elements of an unfair competition claim, as Plaintiff has alleged that the Non-debtor Defendants are manufacturing and selling imitation goods that have been made to appear – by way of the use of the M&C Apparel's patterns, markers and trademarks – as genuine.

III. CONCLUSION

For the reasons set forth above, Plaintiff FTC Commercial Corp. respectfully requests that the Court *deny* Defendants' Motion in its entirety, and order them to file an Answer to the Complaint forthwith.

Dated: March 12, 2009

Respectfully submitted,

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